Forbes

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"Siff-ting" through the Family Business: I untangle the problems.

ENTREPRENEURS

Your Unprofitable Customers Are Killing You

How many of your clients are unprofitable? My guess is you have no idea. If your business overall is profitable, you're not worrying too much about the unprofitable ones. And you should. We have a client that is a family business with 1,100 total customers. This client was shocked to find out that 350 of their customers were unprofitable. And so were we. Unprofitable customers resulted in a two million dollar loss to their bottom line.

Quite simply, unprofitable customers consume more resources than they pay for. They divert attention from a company's profitable customers, and they create tension between the sales team, who is looking to generate revenue, and management, who is keeping an eye on profitability.

So what's a company to do about unprofitable customers? Here are 10 tips.

DO NOT:

1. Do not implement an across-the-board price increase. You could end up having to raise prices so much to make up for the losses that there's no way you could really justify the hike. The consequence will be losing some of your profitable customers.

2. Do not selectively allocate costs. Twenty-five percent of sales does not mean twenty-five percent of overhead. You've got to allocate costs based upon what activities match up with the client. Another client of ours had two brands—one of which was far more profitable. They decided to allocate 70% of the cost of servicing their customers of the more profitable brand. The problem was the sales people were spending 70% of their time on the brand that only generated 30% of the profits. This kind of selective allocation distorts the true picture of profitability.

3. Do not be emotional. Your decision process needs to be data-driven. Recently, when we recommended that our client drop an unprofitable customer, the client told us, 'What do you mean? He's been my customer for over ten years now.' The real issue is, 'how long has the account been unprofitable for you?'

4. Do not confuse profit and revenue. Just because a customer is filling your top revenue line doesn't mean that they're impacting your bottom line. It's easy to get enticed by the big revenue figures and forget to do the analysis. You need to analyze customers in terms of driving both your top and bottom line (profit driven volume).

DO:

1. Sell the company additional services or products to attain profitability. We have found that many times customers are not aware of all the services a provider offers. Some clients can be taken from unprofitable to profitable just by educating them on the other items or services you can provide.

2. Raise your price levels selectively. There may be some unprofitable customers who can absorb price increases. You can also raise prices on profitable customers but make sure you are not doing it to make up for the unprofitable ones.

3. Examine whether you are over-servicing customers. Anytime you're servicing a customer there is an associated cost. Do you really need to call on that customer once a month? Maybe once a quarter, or once every two months would do.

4. Separate unprofitable customers into two categories; high-touch and low-touch. Figure out who is requiring a lot of your time compared to who is requiring less. You may be over-servicing unprofitable customers but additionally you need to ask, 'Are these accounts unprofitable because of your existing overhead?' Once you understand what is the cause of their lack of profitability you can determine the best course of action. You may be able to have your customers serviced from a part of your company that has a lower overhead.

5. Sell off unprofitable customers, even to a competitor. If you can't make money off of them, someone else might be able to. If your company is doing $100,000,000 in sales and you have competitors doing $15,000,000 in sales with much lower overhead structures, they might love these $5,000 accounts. The result could be a one-time profit gain for your company plus the benefit of eliminating your unprofitable customers.

6. Test, test, test. Test all changes on a small sample of customers. Go through the pitch with thirty accounts and see what their reaction is when you say, "We're looking at doing XYZ." If you get a positive reaction from the majority, then you know it will work.

There are two final things you should bear in mind. The first is that these approaches are not mutually exclusive. Any and all can be tried simultaneously. The second is that there are times it makes sense to keep unprofitable customers, such as influencers or thought leaders who will help you gain credibility in the marketplace and, hopefully, other customers. If you get a customer that is desirable to other customers (an influencer), you can leverage this customer to gain an additional four to five accounts–that has to be taken into consideration. You can't always assign a dollar figure to the value of an influencer. There are times you will have to make a judgment call as to whether you think this company/customer will be or could be an influencer.

Additionally, you have to understand the impact of your decisions. We had a client who decided to drop certain items from their product line because they were unprofitable. We recommended that they test their idea on their customers. In doing so, they discovered that there was an inter-relationship between those products and some very profitable ones. If they had discontinued the unprofitable items, the result would have been an overall loss of profitability. Therefore, those unprofitable items were similar to the 'influencer' mentioned above where there were other, valid reasons to continue to carry these items.

So don't take the easy way out by raising prices across the board. You have to thoroughly analyze your accounts, take a strategic approach and consider all your options to maximize your overall profitability.

This article is available online at:

http://www.forbes.com/sites/lawrencesiff/2012/05/21/your-unprofitable-customers-are-killing-you/

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